

# Early Retirement — SHB 2180, 03 Session

## Background

SHB 2180 created an early retirement window between September 1, 2003 and February 20, 2004. Public Employees' Retirement System (PERS) plan 1 members retiring during the window could elect to withdraw their employee contributions in a lump sum and receive a reduced monthly benefit. PERS plans 2/3 and State Employees' Retirement System (SERS) plans 2/3 members retiring during the window with 60 years of age and at least 5 years of service could retire with a 3% per year reduction in their benefit. All PERS and SERS members retiring during the window would receive an additional \$10 per month per year of service for the first 24 months of retirement.

PERS and SERS members who retire under this bill and return to work with a PERS or SERS employer would have their retirement allowance reduced 5.5% for each 8 hours worked per month for a maximum reduction of 100%.

## Committee Activity

### Presentation:

December 16, 2003 – Full Committee Meeting

## Recommendation to Legislature

None

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# Select Committee on Pension Policy

## Early Retirement

### (SHB 2180, 03 Session)

*(December 10, 2003)*

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#### **Issue**

SHB 2180 from the 2003 Legislative Session would have allowed PERS 1 members retiring between September 1, 2003 and February 29, 2004, to elect to withdraw their employee contributions in a lump-sum and receive a reduced monthly benefit. Members of PERS 2/3 and SERS 2/3 who were at least 60 years of age and had at least 5 years of service could have retired during the window with a 3% per year reduction in their benefit. All PERS and SERS members retiring during the window would have received an additional \$10 per month per year of service for the first 24 months of retirement.

PERS and SERS members who retire under this bill and return to work with a PERS or SERS employer would have their retirement allowance reduced 5.5% for each 8 hours worked per month for a maximum reduction of 100%.

#### **Staff**

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#### **Members Impacted**

About 10,100 active PERS 1 members would have been affected by SHB 2180. Of this total, about 1,300 members were 65 years of age or older and about 8,800 were under the age of 65. The bill required that PERS 1 members be eligible to retire to benefit under the bill.

Approximately 8,800 PERS 2/3 members would have been affected by this bill. Of this total, about 2,300 members were 65 years of age or older; 1,700 were between the ages of 60 and 64 and had 20 years of service or more; and another 4,800 members were between the ages

of 60 and 64 and had less than 20 years service (but more than 5 years of service). The bill required that PERS 2/3 members be at least age 60 with at least 5 years of service to benefit under the bill.

Approximately 3,900 SERS 2/3 members would have been affected by this bill. Of this total, about 1,100 members were 65 years of age or older; 600 were between the ages of 60 and 64 with 20 years of service or more; and another 2,200 members were between the ages of 60 and 64 and had less than 20 years service (but more than 5 years of service). The bill required that SERS 2/3 members be at least age 60 with at least 5 years of service to benefit under the bill.

### **Current Situation**

Currently, PERS 1 members may retire with an unreduced benefit at age 60 with 5 years of service, at age 55 with 25 years of service, or at any age with 30 years of service.

Members of PERS 2 and SERS 2 may retire with an unreduced benefit at age 65 with 5 years of service. They are also eligible for a reduced benefit at age 55 if they have at least 20 years of service. PERS 2 and SERS 2 members who retire at age 55 with at least 30 years of service receive a 3% reduction for each year that their retirement age precedes age 65. Members who retire with at least 20 years of service, but less than 30 years of service, receive a larger actuarial reduction for early commencement of their benefit.

PERS 3 and SERS 3 members may receive the defined benefit portion of their retirement allowance at age 65 with 10 years of service, at age 65 with 5 years of service if 12 months of that service was earned after age 54, or at age 65 with 5 years service if that service was earned

in Plan 2. They may also receive a benefit at age 55 with 30 years of service with the benefit reduced 3% per year for each year that their retirement age precedes age 65. They may also receive a benefit at age 55 with 10 years of service with the benefit actuarially reduced for each year that their retirement age precedes age 65.

### **History**

Originally HB 2180 provided the early retirement window described above for PERS Plans 1, 2, and 3 only. SHB 2180, a substitute bill, provided the early retirement window for SERS Plans 2 and 3 as well as the PERS Plans included in the original bill. The bill did not pass in the House.

### **Policy Analysis**

Early retirement windows are often touted as a means to achieve fiscal savings by reducing payroll costs. While some temporary salary savings may be realized, they seldom compare favorably with the resulting increased liabilities to the retirement system.

Also, an issue paper entitled "Early Retirement Windows" is attached. For an in-depth policy discussion of early retirement windows, see pages 7-15 of the issue paper.

### **Options**

Only one option is presented to the Committee at this time.

### **Fiscal Impact of Options**

SHB 2180 provided that the PERS 2 and SERS 2 employee contribution rate would not be impacted by the legislation. See the attached fiscal note which details the employer impact.

**Administrative Impact (DRS)**

Input requested.

**Executive Committee Recommendation**

The Executive Committee has forwarded this item to be heard by the full Committee.

**Bill Draft**

SHB 2180 from the 2003 sessions is attached.

**Fiscal Note**

See attachment.

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# Early Retirement Windows



**Joint Committee on Pension Policy**  
*Presented May 21, 1998*

*Prepared by:*

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## Situation Summary:

The issue of early retirement continues to be a topic of interest for legislators, governmental agencies and individual members. This report updates information contained in the 1996 early retirement report and presents policy issues related to targeted early retirement windows.

## Background:

### Early Retirement Windows and Retirement Incentives:

Normal retirement is what occurs after a member has fulfilled the requirements for receiving an unreduced benefit from their retirement system. Eligibility for normal retirement in the Washington retirement systems varies among the systems and Plans.

Members of the Public Employees' Retirement System Plan 1 (PERS 1 and the Teachers' Retirement System Plan 1 (TRS 1) can qualify for an unreduced benefit by meeting one of three combinations of age and/or service. Washington State Patrol (WSP) members must meet one of two combinations of age and/or service. Members of the Law Enforcement Officers' Retirement System Plan 1 (LEOFF 1) must earn at least five years of service and reach a specific age. These same requirements apply to members of the Plan 2 and Plan 3 systems.

In addition to normal retirement, the Plan 2 systems provide members with an on-going opportunity to retire early. The benefit provided by this option is actuarially reduced to reflect the additional years the member will receive payments. **Table #1** provides the eligibility requirements for each of the major Washington retirement systems.

**TABLE #1**  
**Washington Retirement Systems' Retirement Criteria**

<u>System</u>	<u>Plan 1</u>	<u>Plan 2</u>	<u>Plan 3</u>
<b>LEOFF</b>	Age 50/5 YOS	Age 55/5 YOS *Age 50/20 YOS	NA
<b>PERS</b>	Age 60/ 5 YOS Age 55/25 YOS Any Age/30 YOS	Age 65/5 YOS *Age 55/20 YOS	NA
<b>TRS</b>	Age 60/5 YOS Age 55/25 YOS Any Age/30 YOS	Age 65/5 YOS *Age 55/20 YOS	Age 65/5 YOS *Age 55/10 YOS
<b>WSP</b>	Any Age/25 YOS Age 55/5 YOS		

\* Benefit reduced from age 65.

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For purposes of this report, early retirement is discussed in terms of a temporary opportunity (window) allowing certain members to leave employment before normal retirement and begin receiving an unreduced benefit immediately. Early retirement is **not** considered in the context of:

- ◆ Lowering the normal retirement age; or
- ◆ A permanent option allowing members to retire earlier with a reduced benefit. (As exists in the Plan 2 retirement systems.)

There are two types of early retirement windows (ER windows) "blanket" and "targeted". Blanket programs provide early retirement to a large segment of the membership. Usually blanket windows are offered to all members of a retirement system who meet certain age and service requirements. Targeted windows are programs offered to a much smaller group of members, for instance, the employees of a particular agency or facility.

The primary difference in the two types of windows is the scope of the offering. Both blanket and targeted windows are designed to achieve the same end: the voluntary termination of members close to retirement.

In the past, Washington has provided six programs to stimulate retirement among members. While the goals of these programs have varied, all have targeted members of the Public Employees' Retirement System Plan 1 (PERS 1) and/or Teachers Retirement System Plan 1 (TRS 1).

In addition to ER windows, Washington has also employed incentives to encourage members to leave service. As used in the past, incentives are cash payments or increases in salary offered to members already eligible to retire in exchange for the member's agreement to leave service within a certain time period. In other states, incentives have been combined with early retirement to increase the attractiveness of a program. A common combination is to allow members to retire a few years early and credit them with one additional year of service for every X number of years of service already earned.

### **History of Incentives and Early Retirement Programs:**

Incentives and retirement programs offered in the past have been driven by personnel concerns. The goals of these programs can be divided into three categories:

- ◆ Easing adverse impacts on members employed by an abolished agency.
- ◆ Encouraging members close to, or already eligible for retirement, to do so.
- ◆ Reducing FTE's and compensation costs.

**Table #2** is a summary of the six programs. A more complete description is contained in **Appendix B**.

**TABLE #2**  
**Incentives and Early Retirement Windows**  
**Offered in Washington State**

<b>Year</b>	<b>Program</b>
<b>1973</b>	<b>Northern State Hospital</b> When the state decided to close Eastern Washington Hospital, Chapter 43.130 was enacted to provide affected personnel with three options: <ul style="list-style-type: none"> <li>* Relocate to other state employment;</li> <li>* Receive termination pay; or</li> <li>* Members age 55 with five years of service could retire without actuarial reduction in the benefit amount. Members age 45 with 5 years of service could retire with a benefit actuarially reduced from age 55.</li> </ul>
<b>1982</b>	<b>Plan 1 Early Retirement Window</b> Revenue shortfalls prompted the Legislature to allow PERS 1 and TRS 1 members to retire up to five years early without an actuarial reduction in benefits. Active members within five years of normal retirement eligibility were targeted. Legislation did not include any restrictions on retirees returning to work.
<b>1992</b>	<b>Community College/K-12 Retirement Incentives</b> TRS 1 members within two years of retirement eligibility were offered additional teaching hours with increased salary if they agreed to waive their rights to tenure at the end of the two years. The increased work hours and salary served to boost the members average final compensation and retirement benefit. The Department of Retirement Systems has since notified employers that such incentives are not reportable as compensation.
<b>1992/ 1993</b>	<b>Plan 1 Early Retirement Windows</b> Educational reform and government streamlining prompted the Legislature to offer PERS 1 and TRS 1 members the opportunity to retire up to five years early without an actuarial reduction in benefits. Eligibility requirements were the same as for the 1982 window. Legislation included restrictions on retirees returning to work.
<b>1995</b>	<b>Department of Transportation Retirement Incentive</b> Certain PERS 1 DOT employees past retirement eligibility were offered cash incentives to terminate employment. Incentive amounts were based on the member's years of service.

### **Retirement Benefit Policies:**

In 1993 the Joint Committee on Pension Policy (JCPP) adopted a set of retirement benefit policies. As a whole, these policies were designed to develop long-term strategies for pension benefits that would best meet the needs of employees, retirees and employers within available resources. These policies do not focus directly to ER windows, but they do establish a framework for considering early retirement issues.

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Three policies inherent in the Plan 2 systems were identified for continuation:

- ◆ All state and local employees should have essentially the same retirement plans;
- ◆ Retiree benefits should have some form and degree of protection from inflation'
- ◆ Costs should be shared equally between employees and employers.

New Plans, or changes to current plans should be based on the following additional policies:

- ◆ Sufficient income after leaving the workforce should be from a combination of Social Security, retirement benefits and employee savings.
- ◆ Employees must take responsibility for insuring they have a sufficient income after retirement.
- ◆ Retirement benefits are intended to provide income after leaving the workforce.
- ◆ Employees who vest and leave should be provided reasonable value toward their ultimate retirement for their length of service.
- ◆ Retirees should have more flexibility in determining the form and timing of their benefit.
- ◆ Plan design should be as neutral as possible in its affect on employees:
  - ◇ It should not inhibit employees from changing careers or employers.
  - ◇ Employees should not be encouraged to stay in jobs they consider highly stressful.
  - ◇ Employees should not be encouraged to seek early retirement.
- ◆ Any new retirement plan shall not exceed the Plan 2 cost.

### **Benefit Funding:**

Retirement benefits are funded by contributions from employees and their employers. In the case of the LEOFF systems, the state also pays a portion of benefit costs. Contribution rates are fixed in statute for Plan 1 and WSP members; and for LEOFF 1 employers. PERS 1 and TRS 1 employers and the state contribute at a rate calculated to properly fund the systems. Since their rates are based on statute and not cost, Plan 1 and WSP members do not pay for increases in benefits. Employers and the state must pay any additional costs.

PERS and TRS Plan 2 members and employers each contribute one half of the total cost of benefits. In LEOFF 2, the state pays 40% of the cost and the remainder is split between members and employers. In this funding approach, members pay one half the cost of benefit increases.

TRS 3 members do not contribute to their defined benefits. Only their employers contribute. Thus, any increases in benefits are paid for by the employer.

**TABLE #3**  
**Contribution Rates Charged as of 9/1/97**

	PERS		TRS			LEOFF		WSP
	Plan 1	Plan 2	Plan 1	Plan 2	Plan 3	Plan 1	Plan 2	
<b>Employee</b>	6.00%	4.65%	6.00%	6.03%	NA	6.00%	8.48%	7.00%
<b>Employer</b>	7.32%	7.32%	11.75%	11.75%	11.75%	6.00%	5.09%	11.05%
<b>State</b>						9.21%	9.21%	

### **Cost-of-living Adjustments:**

When members leave the workforce early, they are expected to spend more years in retirement. The longer a member receives a retirement benefit, the more important cost-of-living adjustments to that benefit become.

Automatic annual cost-of-living adjustments (COLAs) are provided retirees in all of the Washington retirement systems. The Plan 2 and 3 systems all receive the same type of adjustments. The PERS and TRS Plan 1 systems receive adjustments through an annual increase call "the Uniform COLA". LEOFF 1 and WSP retirees each receive increases based on a separate mechanism.

**TABLE #4**  
**Washington Retirement Systems**  
**Overview of Cost-of-living Adjustment Designs**

<u>Plan</u>	<u>COLA Design</u>	<u>When Received</u>
<b>PERS 1/ TRS 1</b>	Automatic annual increases. Increase is a flat-rate amount per year of service. It is increased by 3% each year.	Member has reached age-66 and been retired for one year.
<b>LEOFF 1</b>	Automatic annual adjustment Increase is equal to advances in the Seattle Consumer Price Index.	Member has been retired one year.
<b>All Plans 2/ TRS 3</b>	Automatic adjustment matches advances in the Seattle Consumer Price Index, up to 3% a year.	Member has been retired one year.
<b>WSP</b>	Automatic annual adjustment of 2% of benefit.	Member has been retired one year.

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## Policy Issues:

1. **Early Retirement Windows are a Personnel Tool:** Employers promoting early retirement stress its usefulness as a method for reducing personnel. Employed in this manner early retirement becomes a matter of personnel policy, not retirement policy.
2. **Are Early Retirement Windows an Employee Benefit?** Employees have expressed an interest in leaving public service at a younger age with a retirement allowance. A number of factors outside the pension system directly impact members' ability to maintain their standard of living once they leave the workforce.
3. **The Effect of Early Retirement Windows on the Normal Retirement Age Policy:** Current eligibility for normal retirement is age-65. Allowing early retirement undermines this policy.
4. **Compensation Savings vs. Increases in the Retirement System Costs:** Claims of fiscal savings are often made when early retirement is proposed. While some savings may be realized in compensation costs, early retirement increases liabilities to the retirement system.
5. **Plan 2 Considerations:** Until now all early retirement efforts have been aimed at Plan 1 members. In the future, Plan 2 members will be targeted. Differences in the way benefits in the Plan 1 and Plan 2 systems are funded have significant implications for early retirement windows.

## Analysis:

### 1. Early Retirement as a Personnel Tool:

Temporary early retirement windows and incentives are not prompted by retirement issues. They are tools to address personnel problems. Three common uses are:

- ♦ **When a facility is closed or staff size is greatly reduced.** In loyalty to employees close to retirement, an employer may offer an early retirement program.
- ♦ **To alter the mix of high and low seniority employees who are terminated during a lay-off.** When senior employees retire, it may allow the employer to reduce cut-backs among shorter-term employees.

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- ◆ **To foster innovation.** Shorter-term employees may be more open to new employer initiatives. Encouraging retirement of longer-term employees may prune "dead wood".

None of these uses stem from retirement issues. In fact, they may be counter-productive to retirement policies adopted by the JCPP in 1992. In employing ER windows, the employer must judge the benefits gained from employees leaving the workforce against the pressure it places on retirement benefit goals.

ER programs also have the potential to create personnel problems. Employers have a limited control over who takes advantage of an ER opportunity. The employer can set requirements for eligibility, but it is the individual employee's decision whether to take advantage of the offer. Difficulties arise when a greater or lesser number of employees may decide to retire than anticipated further impacting staffing levels. A second danger of such programs is that critical employees may choose to retire, disrupting the provision of services or the completion of projects. Short time periods for taking advantage of a window further exacerbate this problem.

## **2. Early Retirement as an Employee Benefit:**

There are employers who view ER windows as a periodic supplemental benefit. They see early retirement not only as a means to aid themselves, but also provide older employees with a special opportunity to leave service earlier. While this view may be well intentioned, earlier retirement is not always to the long-term benefit of employees.

Workers who retire early face the challenge of maintaining their standard of living over a longer period of time than retirees who leave at normal retirement. In some cases, this may not be an issue. ER windows can be a boon to employees who:

- ◆ Wish to pursue a second career, while receiving income from their first career.
- ◆ Are affected by health disabilities.
- ◆ Have planned to leave the workforce before eligibility and are financially secure.
- ◆ Have access to affordable health care insurance.

PERS 1 members are especially likely to benefit from ER windows. There are no provisions to allow early retirement with a reduced benefit in the Plan 1 systems. In PERS 1, terminated-vested members (those with at least 5 years of service who leave service without withdrawing their contributions), are not eligible to begin drawing an unreduced retirement benefit until age 65. Benefits can be paid at age 60, but are actuarially reduced from age 65. The effect of these provisions is that members who do not continue working until retirement eligibility must either wait to receive their benefits or accept a reduced amount.

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This delay in terminated-vested benefits does not occur in other Washington retirement systems. TRS 1 terminated-vested members, and members of the Plan 2 and Plan 3 tiers, can begin receiving unreduced benefits when they reach eligibility for normal retirement.

Employers may view an ER window as a good solution to a personnel problem, and employees see them as a short cut to the "golden years", but four factors require consideration.

***The reduced size of the retirement benefit:***

Early retirees receive a smaller retirement allowance than they would have if they worked until normal retirement age. An early retiree permanently forgoes additional service credit, as well as potential future salary increases, in lieu of early receipt of the retirement allowance.

***Inflation:***

In Plan 1, cost-of-living adjustments (COLAs) do not begin until the retiree has reached age-66. In previous ER windows offered by the state, retirees could be as young as age 50. This means some benefit purchasing power will be lost to inflation before the retiree becomes eligible for an annual increase. The amount of the loss could be a little or a lot depending on the rate of inflation and the retiree's age.

Fixed benefits and loss of purchasing power bring discontent. The bulk of persons who sought COLAs in the late 1980s and early 1990s were those whose benefits had been eroded by inflation.

***Eligibility for Social Security:***

First eligibility for Social Security now occurs at age 62. This "early retirement" benefit is roughly 80% of the amount a worker would receive at age 65. A public employee who leaves employment early will not be eligible for Social Security for even this reduced benefit for several years. In addition, individuals who do not work up until eligibility are likely to receive a lower benefit.

The age at which the full Social Security benefit is obtained is increasing. **Appendix C** shows how the increase in full benefit eligibility is being implemented. The reduction for retirement at age-62, from Social Security is also rising. The person who retires now at age 62 receives a benefit approximately 20% less than the full retirement benefit. For the person who is age 62 in the year 2022, the benefit will be approximately 30% less than the full retirement benefit.

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### ***The cost of health care insurance:***

At age-65 retirees become eligible for Medicare. Typically the cost of health care insurance is reduced at this age to reflect coverage under the federal program.

**Appendix D** reflects data from the Washington State Health Care Authority rate schedule, effective January 1, 1998. It shows the monthly premium rates for the pre-age 65 retiree only; and the retiree and spouse. The cost of these premiums range from \$143 to \$179 a month for the retiree only; and from \$262 to \$354 for the retiree and spouse.

### **3. The Effect of Early Retirement on Normal Retirement Age Policy:**

A fundamental impact of early retirement programs is the pressure it exerts on normal retirement age policy. The Legislature established that full retirement benefits will not be paid until the member attains age-65. This policy was established in the creation of PERS 2 and TRS 2. It was reinforced in the creation of TRS 3 and SERS 3.

Early retirement is a limited benefit. Only members who meet the eligibility criteria benefit from it, others gain nothing. Members not eligible for one window will create pressure for another. Adding to this, is the fact that the state has offered three large-scale early retirement windows since 1982. The frequency of these past programs has built an expectation of future programs.

At some point, the expectation and frequency of future ER windows undermines normal retirement policy. Where that line falls may be difficult to determine, except in retrospect. At that point, it may be difficult to reverse the trend.

### **4. Fiscal Impacts and Policy:**

A common justification for early retirement is that it saves the employer money by reducing payroll costs. If salary savings do occur, they seldom compare favorably to the increased costs to the retirement systems. The fiscal impact of ER windows is to temporarily lower payroll costs, while increasing retirement system liabilities. Agencies also experience impacts from unbudgeted cash-outs of unused employee leave.

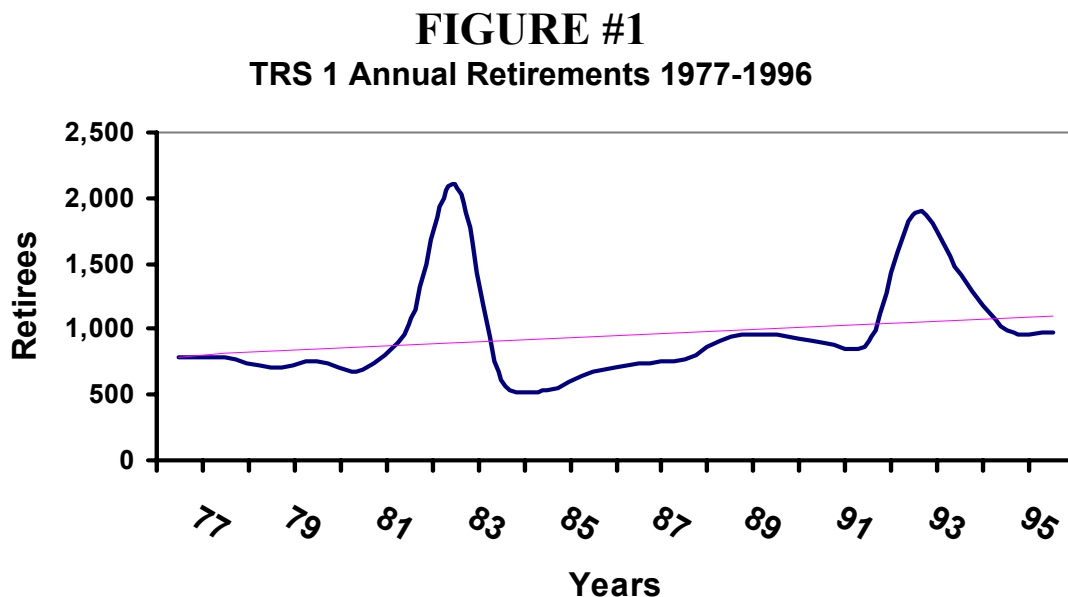
#### ***Compensation Savings:***

The "compensation savings" theory of ER windows is relatively straightforward. Windows encourage senior employees, who are earning relatively high salaries, to leave employment. These employees are then replaced by employees earning lower salaries. The difference between the senior employee's salary and the replacement's salary constitutes a savings for the employer.

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The replacement of personnel that occurs as a result of ER windows is the same one that occurs when an individual reaches normal retirement. The only difference between early and normal retirement is timing. With an ER window, a large group of employees may leave at one time. Any savings that are realized in a window are simply realized all at once instead of over a period of time. Nothing happens in an ER window that would not have happened within the next few years as workers become eligible for normal retirement.

**Figure #1** shows TRS 1 retirements from 1977 through 1995 and a retirement trend line. There are peaks when an ER window is offered and in subsequent years, subnormal retirements occur. The ER window has "borrowed" retirees from the next five years, when those employees would have reached eligibility under normal retirement rules.



Though easy to understand in theory, the cost savings of ER windows are difficult to demonstrate in practice. A number of factors complicate this calculation.

- ◆ **Replacement salaries** In theory, an ER window replaces a high-paid employee, with a low-paid one. In practice, it is usually an employee who is already close in pay to the retiree who moves into that position. This sets off a series of promotions within the agency and eventually an entry-level employee is hired. To calculate the "savings" does the analyst use the salary of the new hire, or the worker who actually replaced the retiree?
- ◆ **Rate of replacement** Real salary savings occur only if the retiree is not replaced. This rarely happens except in situations where a facility closes or agency is abolished. Assumptions about the length of time a retiree's position will go unfilled impact the estimation of compensation savings.

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- ◆ **Training costs** Replacement employees may need additional training to perform their new responsibilities. Should these costs be included in the savings calculation?

The only salary data available regarding Washington's ER windows comes from the 1992 program. The Office of Financial Management (OFM) had agencies report their savings after the retirement of their employees. OFM estimated the state saved approximately \$1 million in salary savings from PERS 1 early retirees and approximately \$8.6 million from TRS 1.

The Office of the State Actuary (OSA) also conducted a study of the 1992 early retirement window. From the data it received, it was estimated that from \$90,000 to \$400,000 was saved in salaries as a result of PERS 1 retirees and between \$7.2 million and \$16.8 million was saved as a result of TRS 1 retirees. The variability of results from the two studies underscores the difficulty of calculating savings.

Whatever savings may be attributed to an ER window, they are only effective in the current fiscal period. Economies in government are not accumulated from one budget cycle to the next.

#### ***Actuarial Impacts:***

Except in LEOFF 1, service retirement is the most expensive element of the state's retirement system. Early retirement increases this cost by providing additional years in retirement, while shortening the funding period. **Tables #5 and #6** provide a relative breakdown of benefit costs without an ER window.

**TABLE #5**  
**Distribution of Plan 1 Retirement Costs**

<b><u>Benefit</u></b>	<b><u>PERS 1</u></b>	<b><u>TRS 1</u></b>	<b><u>LEOFF 1</u></b>
<b>Service Retirement</b>	86.1%	90.2%	26.8%
<b>Disability</b>	2.2%	1.3%	67.2%
<b>Death</b>	1.1%	0.6%	3.2%
<b>Withdrawal</b>	10.6%	7.9%	2.9%
<b>Total</b>	100.0%	100.0%	100.0%

**TABLE #6**  
**Distribution of Plan 2 Retirement Costs**

<u>Benefit</u>	<u>PERS 2</u>	<u>TRS 2</u>	<u>LEOFF 2</u>
Service Retirement	84.4%	89.9%	94.2%
Disability	1.8%	0.7%	0.6%
Death	1.2%	0.5%	0.4%
Withdrawal	12.7%	8.9%	4.8%
<b>Total</b>	100.0%	100.0%	100.0%

**Table #7** shows employer costs for the early retirement programs of 1982, 1992 and 1993. The amounts shown are for the first biennial period only. They are represented in 1996 dollars. Increases in contributions rates to fund these programs are applied to all earnable compensation and will be paid by all employers through June 30, 2024.

**TABLE #7**  
**Actuarial Costs for Early Retirement**  
**Programs in 1982, 1992 and 1993**  
*(\$ in Millions)*

		2-Year Cost		25-Year Cost		Unfunded Accrued Actuarial Liability
		General Fund-State	All Funds	General Fund-State	All Funds	
<b>1982</b>						
PERS 1	1,416	\$ 1.1	\$ 4.1	\$ 28	\$ 107	\$ 36.7
TRS 1	1,023	3.4	4.2	84	104	40.5
<b>1992</b>						
PERS 1	1,198	0.7	2.7	19	73	31.0
TRS 1	818	2.9	3.6	72	89	32.3
<b>1993</b>						
PERS 1	867	0.7	2.7	19	73	22.4
TRS 1	410	1.4	1.7	36	45	16.2

As a matter of comparison, salary data collected by OFM and OSA estimated compensation savings for the 1992 ER program between \$8 and \$17.2 million for PERS 1 and TRS 1 combined. The present value of the unfunded liability incurred by the 1992 ER window was \$63.3 million.

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### ***Terminal pay and cash-outs:***

When employees retire, they are often eligible to receive cash payments for unused annual leave, sick leave and other benefits. Some of these payments can be quite large. When an ER window is offered, a large group of employees may leave an agency within a short time. The cost of unanticipated cash-outs can be disruptive to an agency and may put its programs into jeopardy in the short run.

## **5. Plan 2 Considerations:**

To date, ER windows have only targeted members of the PERS and TRS Plan 1 systems. These plans have been closed to new members for 22 years. The bulk of Washington's public employees now belong to Plans 2 and 3. If employers are going to continue to use ER windows to manage their workforces, they will have to begin offering them to Plan 2 and 3 members. Key differences in these tiers' benefit structures introduce additional policy issues.

### ***Funding:***

In the Plan 1 tiers, members pay a fixed contribution rate. In the Plan 3 tiers, the member does not contribute to the defined benefit portion of the retirement benefits. In both Plans, any increases in benefits, such as an ER window, would be paid for with an increase in employer contributions.

The Plan 2 tiers present a different situation. Benefit costs are split evenly between the employer and the employee. When the cost of benefits increase, both are required to contribute more. If an ER window is offered in Plan 2, both employers and employees will see contributions rise. Non-eligible members would be expected to pay for the program even though they cannot benefit from it.

### ***Retirement Age:***

Plan 1 members have three options for meeting retirement eligibility:

- ◆ Age 60 with 5 years of service;
- ◆ Age 55 with 25 years of service; or
- ◆ Any age with 30 years of service.

These age and service options produce retirees at a range of ages roughly from 49 to 60 years. When ER windows are targeted as they have been, by reducing eligibility 5 years, they produce retirees who range in age from 45 to 55.

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In contrast to the Plan 1 tiers, eligibility for normal retirement in Plan 2 is age-65. Lowering eligibility 5 years brings that number to age 60. An ER window of this design only affects older members. A program aimed at this population may be viewed as age-discriminatory.

### ***Reduction Factors for the On-going Early Retirement Benefit:***

Plan 2 members have a permanent option to retire with a reduced benefit at age 55 with 25 years of service. (See **Table #1**.) An ER window targeted to Plan 2 members will have to determine an equitable policy for members who wish to retire under this eligibility during the ER window. If a window is designed as the Plan 1 windows have been, Plan 2 members could retire at age-60 with 5 years of service:

- ◆ Does this mean that members who are age 50 with 15 years of service qualify for the on-going reduced early retirement benefit during the open window?
- ◆ Do members who meet the age-60 requirement see their benefit reduced from age 60, rather than the normal retirement age of 65?
- ◆ Should the members who are retirement eligible under the on-going early retirement option receive any incentives to retire during a ER window ?

## **Policy Questions:**

There are several policy questions that might be considered with regard to early retirement programs. Two general areas to consider are: the early retirement program itself and responsibility for funding the program.

### **Early Retirement Program Design:**

- ◆ Should early retirement continue to be used as an ad hoc supplemental retirement benefit?
- ◆ Should the Joint Committee adopt a set of guidelines to be used if future early retirement programs are offered?
- ◆ Should early retirement be established as a permanent program to be initiated by the employer?
- ◆ Should early retirement be targeted to identified employee categories?

### **Early Retirement Program Funding:**

- ◆ Should payment continue to be made by all employers or only by those employers affected by early retirement?
- ◆ Should payment of the costs of early retirement be amortized or paid immediately?

# Appendix A

## Washington State Retirement Systems Membership by Age and Years of Service

### PERS 1 Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	1,215	499	271	88	38	2,111
5 - 9	1,791	843	420	204	59	3,317
10 - 14	1,869	999	566	262	66	3,762
15 - 19	2,168	1,184	868	412	101	4,733
20 - 24	5,748	3,413	2,333	1,163	277	12,934
25 - 29	1,469	2,433	1,262	709	191	6,064
30 or More	41	389	476	278	105	1,289
Total	14,301	9,760	6,196	3,116	837	34,210

### PERS 2 Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	51,743	4,577	1,990	994	466	59,770
5 - 9	37,823	6,097	2,939	1,442	550	48,851
10 - 14	16,770	4,355	2,573	1,293	385	25,376
15 - 19	8,240	2,747	1,916	1,184	300	14,387
20 - 24	2	6	4	2	1	15
25 - 29	0	1	0	0	0	1
30 or More	0	0	0	0	0	0
Total	114,578	17,783	9,422	4,915	1,702	148,400

\* Boxed areas indicate eligibility for normal retirement.

## TRS 1 Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	319	188	59	13	2	581
5 - 9	617	498	150	42	14	1,321
10 - 14	878	653	225	50	11	1,817
15 - 19	2,087	783	402	118	20	3,410
20 - 24	4,336	1,811	769	283	45	7,244
25 - 29	1,418	3,219	1,164	368	81	6,250
30 or More	2	700	891	415	85	2,093
Total	9,657	7,852	3,660	1,289	258	22,716

## TRS 2 Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	12,652	804	257	66	17	13,796
5 - 9	10,626	1,142	380	122	23	12,293
10 - 14	5,228	813	385	115	19	6,560
15 - 19	3,017	580	304	130	29	4,060
20 - 24	0	0	0	0	0	0
25 - 29	0	0	0	0	0	0
30 or More	0	0	0	0	0	0
Total	31,523	3,339	1,326	433	88	36,709

\* Boxed areas indicate eligibility for normal retirement.

## LEOFF 1 Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	2	0	1	0	0	3
5 - 9	6	0	0	0	0	6
10 - 14	6	4	1	0	0	11
15 - 19	143	16	0	0	0	159
20 - 24	960	270	28	1	0	1,259
25 - 29	258	593	129	13	0	993
30 or More	1	74	59	26	2	162
<b>Total</b>	1,376	957	218	40	2	2,593

## LEOFF 2 Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	3,306	50	20	3	0	3,379
5 - 9	3,275	62	17	9	1	3,364
10 - 14	1,961	86	34	7	0	2,088
15 - 19	1,842	124	20	7	1	1,994
20 - 24	2	0	0	0	0	2
25 - 29	0	0	0	0	0	0
30 or More	0	0	0	0	0	0
<b>Total</b>	10,386	322	91	26	2	10,827

\* Boxed areas indicate eligibility for normal retirement.

## WSP Membership by Age and Years of Service 1996 Valuation Data

Years of Service	49 or Less	50-54	55-59	60-64	65 or Older	Total
0 - 4	94	0	0	0	0	94
5 - 9	294	2	0	0	0	296
10 - 14	174	1	0	0	0	175
15 - 19	110	3	1	0	0	114
20 - 24	97	16	0	0	0	113
25 - 29	50	48	6	0	0	104
30 or More	0	10	11	0	0	21
<b>Total</b>	819	80	18	0	0	917

\* Boxed areas indicate eligibility for normal retirement.

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# Appendix B

## Prior Retirement Incentives and Windows

### 1973 - Northern State Hospital:

In 1973, the Department of Social and Health Services determined Northern State Hospital was no longer needed as an institution for the mentally ill. As a consequence, the decision was made to permanently close the facility.

Chapter 43.130 RCW was enacted to address this situation and remains in effect today. Under these provisions, qualified personnel of an affected institution are given three options:

- ◆ Relocate to other state employment;
- ◆ Receive payment of termination pay; or
- ◆ If an affected employee has attained age 55 and completed at least 5 years of service, receive a retirement allowance without actuarial reduction. If, an affected employee is age 45 with at least 5 years of service, he or she could retire with an actuarially reduced benefit.

The allowance offered under this Chapter is limited. No allowance can be received in a year following a year in which the retiree earned more than \$6,000. The \$6,000 amount is annually adjusted by any COLA received by PERS retirees, beginning in 1973. (Factually, this is an impossible task, given the nature of COLAs provided from 1973 through the present.)

### Community College/K-12 Retirement Incentive Programs:

In June of 1992, the JCPP learned of several retirement incentive programs in operation within the community college districts. A TRS 1 member who was eligible to retire within two years could sign an agreement to retire in two years and waive their rights of tenure at the end of that period. In consideration for this agreement, the member would receive summer session contracts for a class load 50 percent greater than the standard summer load with compensation 72 percent greater than standard compensation.

Certain school districts were also providing retirement incentives. In these instances, the teachers were being given additional teaching days if they agreed to retire within a certain period of time

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In both cases, not only were the faculty member and teacher receiving increased compensation, they were also enhancing their average final compensation (AFC), which in turn increased their retirement benefit. DRS later issued a notice to community college and K-12 districts informing them this type of practice was not condoned and such incentives were not reportable as compensation.

## Department of Transportation Retirement Incentive Program:

In 1995, the Department of Transportation was experiencing personnel and morale problems in one of its regional offices. Part of the problem was caused by the continued longevity of professional engineering employees. These individuals were not retiring as anticipated and the agency's promotional patterns were being stymied. In addition, budgetary cutbacks were expected.

DOT successfully proposed an incentive program to the Governor and the Legislature. The legislation allowed DOT to offer a \$500 cash bonus for each year of service to certain employees if they agreed to retire. The incentive program was initiated in 1996 for PERS 1 employees of DOT's Southwest Region who were already eligible to retire. Twenty-three employees were eligible for the bonus. Thirteen accepted it. The enabling legislation for this incentive expired in 1997.

## 1982 Early Retirement Window:

In 1982, the state was experiencing fiscal problems. With declining revenues, the Legislature faced the prospect of reductions in programs and FTEs. To minimize the impact of personnel reductions and realize short-term salary savings, an early retirement program was offered to PERS and TRS Plan 1 members.

In **Table #1**, the qualifications for normal retirement are compared with the qualifications for the early retirement window. (The term *normal retirement* means the receipt of the retirement allowance without reduction.)

**TABLE #1**  
**Eligibility for 1982 Early Retirement**  
**PERS 1 and TRS 1**

<b>Normal Retirement</b>	<b>Early Retirement</b>
Age 60 with 5 years of service	Age 55 with 5 years of service
Age 55 with 25 years of service	Age 50 with 20 years of service
30 years of service	25 years of service

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Normal retirement qualifications were simply reduced by five years. **Table #2** provides some statistics for the 1982 program.

**TABLE #2**  
**1982 Early Retirement Statistics**

	<b>PERS 1</b>	<b>TRS 1</b>
Number of Retirees	1,938	1,023
Average Age	56.2	53.8
Average Service	18.3	22.6
Years to Normal Retirement	2.3	2.2
Percent of Those Eligible to Utilize Early Retirement	22%	29%

There was an additional element connected with the 1982 early retirement program which may have effected participation rates. The Legislature had just adopted language which prospectively eliminated any cash-out of unused leave, for PERS 1 members. The elimination of this benefit would have prevented PERS 1 members from applying a portion of their cash-out to their average final compensation (AFC) and retirement benefit. The language to eliminate cash-outs was later declared unconstitutional. Nonetheless, a large number of members may have taken advantage of early retirement to ensure they would be able to use their cash-outs in calculating their AFC.

In terms of saving money, the 1982 early retirement program contained one flaw. It did not prohibit early retirees from contracting with their employers to do the same job they were doing prior to retirement. A significant number of retirees did just that and no cost savings were realized.

## **1992/1993 Early Retirement Window:**

The early retirement programs for the years 1992 and 1993 (treated here as a single program), were enacted for two reasons. First, during this period, educational reform was an area of intense legislative deliberation. Some maintained that an early retirement program would provide longer service teachers with the opportunity to retire. By so doing, openings would then be available to younger teachers who might be more amenable to change. Second, it was possible RIFs might be used to trim the size of government. Together these possibilities supported providing an early retirement program.

The time periods for the 1992 and 1993 open windows are shown in **Table #3**.

**TABLE #3**  
**Operative Dates for Early Retirement**

	<b>Employed in an Eligible Position</b>	<b>Application Submitted By</b>	<b>Retire By</b>
<b>1992</b>	April 2, 1992	June 15, 1992	August 31, 1992
<b>1993</b>	March 1, 1993	July 1, 1993	August 31, 1993

Eligibility for these programs was identical to the criteria applied in 1982. **Table #4** provides the number of early retirees in the 92/93 programs, as well as the utilization rate.

**TABLE #4**  
**Number of Early Retirees**

	<b>1992</b>			<b>1993</b>		
	Eligible	Retired	Utilization Rate	Eligible	Retired	Utilization Rate
PERS 1	9,381	1,198	12.8%	9,145	867	9.5%
TRS 1	<u>6,611</u>	<u>826</u>	12.5%	<u>6,443</u>	<u>423</u>	6.6%
Total	15,992	2,024	12.7%	15,588	1,290	8.3%

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# Appendix C

## Future Eligibility for Social Security Benefits

### Age Eligible for Full Social Security Benefit

<b>If Born In</b>	<b>Will Be Age 62 In</b>	<b>Age For Full Benefit</b>
1937 or Earlier	1999 or Earlier	65 Years
1938	2000	65 Years 2 Months
1939	2001	65 Years 4 Months
1940	2002	65 Years 6 Months
1941	2003	65 Years 8 Months
1942	2004	65 Years 10 Months
1943-1954	2005-2016	66 Years
1955	2017	66 Years 2 Months
1956	2018	66 years 4 Months
1957	2019	66 years 6 months
1958	2020	66 years 8 Months
1959	2021	66 years 10 Months
1960 or Later	2022 or Later	67 Years

# Appendix D

## 1997 Monthly Premium Rates for Non-Medicare Eligible Retirees

Provider	Retiree Only	Retiree & Spouse	Provider	Retiree Only	Retiree & Spouse
Comm Hlth Plan	\$156.43	\$308.57	PacificCare	\$155.24	\$306.19
Group Health	160.12	315.95	QualMed	166.05	327.81
HealthPlus	178.95	353.81	Regence	179.64	354.99
HMO WA	161.29	318.29	Selectcare	157.86	311.43
Kaiser Foundation	146.22	288.15	Skagit Co Medical	143.79	263.29
Kitsap Physcn Svcs	163.23	322.17	<b>Uniform Medical</b>	158.29	312.29
Medical Svcs Corp	158.20	312.11	Virginia Mason	143.29	262.29
NYLCare	146.66	289.03	Whatcom Med Bureau	143.79	283.29
Options Hlth Care	162.64	320.99			

# FISCAL NOTE

REQUEST NO.

RESPONDING AGENCY:

CODE:

DATE:

BILL NUMBER:

**Office of the State Actuary**

**035**

**03/12/03**

**SHB 2180**

## SUMMARY OF BILL:

This bill impacts the Public Employee's Retirement System (PERS) and School Employee's Retirement System (SERS) by offering retirement incentives to members retiring between September 1, 2003 and February 29, 2004.

PERS 1 members who retire during this window may withdraw all or part of their accumulated contributions and receive an allowance actuarially reduced to reflect the monthly annuity which would have been purchased by those contributions.

PERS 2/3 and SERS 2/3 members who have at least 5 years of service and reached at least age 60 would be eligible to retire during the window and receive an allowance reduced 3% per year for the difference in the number of years between their age at retirement and age 65.

PERS and SERS members who retire during this window would also receive a temporary increase in their retirement allowance of \$10 per month for each year of service. This increase would remain in effect for the first 24 months of the member's retirement.

PERS and SERS members who retire under this bill and return to work with a PERS or SERS employer would have their retirement allowance reduced 5.5% for each 8 hours worked per month (for a maximum reduction of 100%).

The PERS 2 and SERS 2 employee contribution rate shall not be impacted by this bill.

Effective Date: 90 days after session.

## CURRENT SITUATION:

Currently, PERS 1 members may retire with an unreduced benefit at age 60 with 5 years of service, at age 55 with 25 years of service, or at any age with 30 years of service.

Members of PERS 2 and SERS 2 may retire with an unreduced benefit at age 65 with 5 years of service. They are also eligible for a reduced benefit at age 55 if they have at least 20 years of service. PERS 2 and SERS 2 members who retire at age 55 with at least 30 years of service receive a 3% reduction for each year that their retirement age precedes age 65. Members who retire with at least 20 years of service, but less than 30 years of service, receive a larger actuarial reduction for early commencement of their benefit.

PERS 3 and SERS 3 members may receive the defined benefit portion of their retirement allowance at age 65 with 10 years of service, at age 65 with 5 years of service if 12 months of that service was earned after age 54, or at age 65 with 5 years service if that service was earned in Plan 2. They may also receive a benefit at age 55 with 30 years of service with the benefit reduced 3% per year for each year that their retirement age precedes age 65. They may also receive a benefit at age 55 with 10 years of service with the benefit actuarially reduced for each year that their retirement age precedes age 65.

## **MEMBERS IMPACTED:**

About 10,100 active PERS 1 members would be affected by this bill. Of this total, about 1,300 members are 65 years of age or older and about 8,800 are under the age of 65. PERS 1 members must be eligible to retire to benefit under this bill.

There are approximately 8,800 PERS 2/3 members who would be affected by this bill. Of this total, about 2,300 members are 65 years of age or older; 1,700 between the ages of 60 and 64 who have 20 years of service or more; and another 4,800 members between the ages of 60 and 64 who have less than 20 years service (but more than 5 years of service). PERS 2/3 members must be at least age 60 with at least 5 years of service to benefit under this bill.

There are approximately 3,900 SERS 2/3 members who would be affected by this bill. Of this total, about 1,100 members are 65 years of age or older; 600 between the ages of 60 and 64 who have 20 years of service or more; and another 2,200 members between the ages of 60 and 64 who have less than 20 years service (but more than 5 years of service). SERS 2/3 members must be at least age 60 with at least 5 years of service to benefit under this bill.

All members who elect to retire under this bill receive \$10 per month for each year of service for the first 2 years of their retirement. PERS 1 members will have the opportunity to retire with a lump sum plus a reduced retirement allowance. PERS 2/3 and SERS 2/3 members under age 65 receive a subsidized 3% early retirement reduction instead of a full actuarial reduction.

The \$10 per month (times years of service) temporary annuity will provide an incentive for all affected PERS and SERS members to retire. The lump sum benefit for PERS 1 members will provide an additional incentive for some affected PERS 1 members to retire. The lump sum benefit, however, will also reduce the amount of their guaranteed retirement allowance (prior to lump sum). The subsidized early retirement reduction factor will provide an additional incentive for affected PERS 2/3 and SERS 2/3 members under age 65 to retire. This incentive will likely vary depending on the amount of the member's retirement allowance in relation to their pre-retirement income. In other words, the larger the retirement allowance, the larger the incentive to retire. All else being equal, the more service a member has at retirement, the larger the retirement allowance.

## ASSUMPTIONS:

The following table contains the retirement probability assumptions utilized in this fiscal note:

System / Plan / Characteristics	Retirement Assumption
Plan 1 (employed and eligible to retire)	50%
Plan 2/3 age 65 and older	Twice the normal rate
Plan 2/3 age 60-64 with 20 or more years of service	100%
Plan 2/3 age 60-64 with less than 20 years of service	Normal rate for those with 20 years of service

## FISCAL IMPACT:

### Description:

For PERS 1, a large part of the cost stems from the election of the affected members to retire earlier than our ongoing assumptions indicate, rather than from any benefits provided under this bill. For PERS 2/3 and SERS 2/3, the costs arise primarily from the extra benefits provided under this bill.

### Actuarial Determinations:

The bill will impact the actuarial funding of the system by increasing the present value of benefits payable under the System and the required actuarial contribution rate as shown below:

(Dollars in Millions)		Public Employees' Retirement System:		
		Current	Increase	Total
<b>Actuarial Present Value of Projected Benefits</b>	PERS 1	\$ 12,244	\$ 102	\$ 12,346
	PERS 2/3	12,428	65	12,493
(The Value of the Total Commitment to all Current Members)	SERS 2/3	1,610	13	1,623
<b>Unfunded Actuarial Accrued Liability</b>	PERS 1	\$ 860	\$ 117	\$ 977
(The Portion of the Plan 1 Liability that is Amortized at 2024)				
<b>Unfunded Liability (PBO)</b>	PERS 1	\$ 301	\$ 148	\$ 449
(The Value of the Total Commitment to all Current Members Attributable to Past Service)	PERS 2/3	(4,874)	128	(4,746)
	SERS 2/3	(724)	22	(702)
<b>Required Contribution Rate (Employer)*</b>	PERS	2.05%	.24%	2.29%
	SERS	1.74%	.24%	1.98%

\*The increase includes .09% for the Plan 1 UAAL and .15% for employer normal cost in Plan 1 or Plan 2/3.

## Fiscal Budget Determinations:

As a result of the higher required contribution rate, the increase in funding expenditures is projected to be:

Effective September 1, 2003	<u>PERS</u>	<u>SERS</u>
<b>Increase in Contribution Rates:</b>		
Employee	0.00%	0.00%
Employer State	0.24%	0.24%

### Costs (in Millions):

#### 2003-2005

##### State:

General Fund	\$ 6.7	\$ 2.8
Non-General Fund	<u>10.7</u>	<u>0.0</u>
<b>Total State</b>	<b>\$ 17.4</b>	<b>\$ 2.8</b>
Local Government	\$ 15.5	\$ 2.4

#### 2005-2007

##### State:

General Fund	\$ 8.1	\$ 3.6
Non-General Fund	<u>13.2</u>	<u>0.0</u>
<b>Total State</b>	<b>\$ 21.3</b>	<b>\$ 3.6</b>
Local Government	\$ 19.0	\$ 3.2

#### 2003-2028

##### State:

General Fund	\$ 166.5	\$ 79.5
Non-General Fund	<u>272.3</u>	<u>0.0</u>
<b>Total State</b>	<b>\$ 438.8</b>	<b>\$ 79.5</b>
Local Government	\$ 389.7	\$ 70.4

## State Actuary's Comments:

The actual cost of this bill will be based on the actual number of affected members who elect to participate in the window. We have not included the impact of transfers from PERS 2 to PERS 3. The impact for the purposes of this fiscal note, however, is negligible.

It is assumed that terminated-vested members are not eligible for this window.

## STATEMENT OF DATA AND ASSUMPTIONS USED IN PREPARING THIS FISCAL NOTE:

The costs presented in this fiscal note are based on our understanding of the bill as well as generally accepted actuarial standards of practice including the following:

1. Costs were developed using the same membership data, methods, assets and assumptions as those used in preparing the September 30, 2001 actuarial valuation report of the Public Employee's Retirement System and School Employee's Retirement System.
2. As with the costs developed in the actuarial valuation, the emerging costs of the System will vary from those presented in the valuation report or this fiscal note to the extent that actual experience differs from that projected by the actuarial assumptions.
3. Additional assumptions used to evaluate the cost impact of the bill which were not used or disclosed in the actuarial valuation report are described in the body of the fiscal note.
4. The analysis of this bill does not consider any other proposed changes to the system. The combined effect of several changes to the system could exceed the sum of each proposed change considered individually.
5. This fiscal note is intended for use only during the 2003 Legislative Session.
6. The funding method used for Plan 1 utilizes the Plan 2/3 employer/state rate as the Normal Cost and amortizes the remaining liability (UAAL) by the year 2024. Benefit increases to Plan 2/3 will change the UAAL in Plan 1. The cost of benefit increases to Plan 1 increases the UAAL.
7. Plan 2/3 utilizes the Aggregate Funding Method. The cost of Plan 2/3 is spread over the average working lifetime of the current active Plan 2/3 members.

## GLOSSARY OF ACTUARIAL TERMS:

**Actuarial Present Value:** The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions (i.e. interest rate, rate of salary increases, mortality, etc.)

**Projected Benefits:** Pension benefit amounts which are expected to be paid in the future taking into account such items as the effect of advancement in age as well as past and anticipated future compensation and service credits.

**Normal Cost:** Computed differently under different funding methods, the normal cost generally represents the portion of the cost of projected benefits allocated to the current plan year.

**Unfunded Actuarial Accrued Liability (UAAL):** The cost of Plan 1 is divided into two pieces:

- The Normal Cost portion is paid over the working lifetime of the Plan 1 active members. The remaining cost is called the UAAL.
- The UAAL is paid for by employers as a percent of the salaries of all Plan 1, 2 and 3 members until the year 2024.

**Pension Benefit Obligation (PBO):** The portion of the Actuarial Present Value of future benefits attributable to service credit that has been earned to date (past service).

**Unfunded Liability (Unfunded PBO):** The excess, if any, of the Pension Benefit Obligation over the Valuation Assets. This is the portion of all benefits earned to date that are not covered by plan assets.

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SUBSTITUTE HOUSE BILL 2180

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State of Washington

58th Legislature

2003 Regular Session

**By** House Committee on Appropriations (originally sponsored by Representatives Romero, Hunt, Sommers, Armstrong, Conway, Kessler, Kenney, Rockefeller and McDermott)

READ FIRST TIME 03/10/03.

1       AN ACT Relating to early retirement; reenacting and amending RCW  
2       41.45.061; adding new sections to chapter 41.40 RCW; and adding new  
3       sections to chapter 41.35 RCW.

4       BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF WASHINGTON:

5       NEW SECTION.   **Sec. 1.** A new section is added to chapter 41.40 RCW  
6       under the subchapter heading "plan 1" to read as follows:

7       (1) Any member retiring between September 1, 2003, and February 29,  
8       2004, may irrevocably elect, at the time of retirement, to withdraw all  
9       or a part of his or her accumulated contributions, other than any  
10      amount paid under RCW 41.50.165, and to receive, in lieu of the full  
11      retirement allowance provided by RCW 41.40.185, a reduction in the  
12      standard two percent allowance, of the actuarially determined amount of  
13      monthly annuity which would have been purchased by the contributions.

14      (2) No member electing the option provided in subsection (1) of  
15      this section may withdraw an amount of accumulated contributions which  
16      would lower his or her retirement allowance below the minimum allowance  
17      provided by RCW 41.40.1984 on the date the withdrawal is made.

18      (3) The monthly retirement allowance of a member electing the

option provided in subsection (1) of this section may be reduced even further pursuant to the options provided in RCW 41.40.188.

(4) If a retiree under this section enters employment with an employer, the retiree's monthly retirement allowance will be reduced by five and one-half percent for every eight hours worked during that month up to a maximum reduction of one hundred percent.

**NEW SECTION.** **Sec. 2.** A new section is added to chapter 41.40 RCW under the subchapter heading "plan 2" to read as follows:

(1) Any member with at least five service credit years who has attained at least age sixty shall be eligible to retire between September 1, 2003, and February 29, 2004, and to receive a retirement allowance computed according to RCW 41.40.620, except that a member retiring under this section shall have his or her retirement allowance reduced by three percent per year to reflect the difference in the number of years between age at retirement and the attainment of age sixty-five.

(2) The monthly retirement allowance of a member retiring under this section may be reduced even further as provided in RCW 41.40.660.

(3) If a retiree under this section enters employment with an employer, the retiree's monthly retirement allowance will be reduced by five and one-half percent for every eight hours worked during that month up to a maximum reduction of one hundred percent.

**NEW SECTION.** **Sec. 3.** A new section is added to chapter 41.40 RCW under the subchapter heading "plan 3" to read as follows:

(1) Any member with at least five service credit years who has attained at least age sixty shall be eligible to retire between September 1, 2003, and February 29, 2004, and to receive a retirement allowance computed according to RCW 41.40.790, except that a member retiring under this section shall have his or her retirement allowance reduced by three percent per year to reflect the difference in the number of years between age at retirement and the attainment of age sixty-five.

(2) The monthly retirement allowance of a member retiring under this section may be reduced even further as provided in RCW 41.40.845.

(3) If a retiree under this section enters employment with an

1 employer, the retiree's monthly retirement allowance will be reduced by  
2 five and one-half percent for every eight hours worked during that  
3 month up to a maximum reduction of one hundred percent.

4 **Sec. 4.** RCW 41.45.061 and 2001 2nd sp.s. c 11 s 13, 2001 2nd sp.s.  
5 c 11 s 12, and 2001 c 180 s 1 are each reenacted and amended to read as  
6 follows:

7 (1) The required contribution rate for members of the plan 2  
8 teachers' retirement system shall be fixed at the rates in effect on  
9 July 1, 1996, subject to the following:

10 (a) Beginning September 1, 1997, except as provided in (b) of this  
11 subsection, the employee contribution rate shall not exceed the  
12 employer plan 2 and 3 rates adopted under RCW 41.45.060, 41.45.053, and  
13 41.45.070 for the teachers' retirement system;

14 (b) In addition, the employee contribution rate for plan 2 shall be  
15 increased by fifty percent of the contribution rate increase caused by  
16 any plan 2 benefit increase passed after July 1, 1996;

17 (c) In addition, the employee contribution rate for plan 2 shall  
18 not be increased as a result of any distributions pursuant to section  
19 309, chapter 341, Laws of 1998 and RCW 41.31A.020.

20 (2) The required contribution rate for members of the school  
21 employees' retirement system plan 2 shall equal the school employees'  
22 retirement system employer plan 2 and 3 contribution rate adopted under  
23 RCW 41.45.060, 41.45.053, and 41.45.070, except as provided in  
24 subsection (3) of this section.

25 (3) The member contribution rate for the school employees'  
26 retirement system plan 2 shall be increased by fifty percent of the  
27 contribution rate increase caused by any plan 2 benefit increase passed  
28 after September 1, 2000.

29 (4) The required contribution rate for members of the public  
30 employees' retirement system plan 2 shall be set at the same rate as  
31 the employer combined plan 2 and plan 3 rate.

32 (5) The required contribution rate for members of the law  
33 enforcement officers' and fire fighters' retirement system plan 2 shall  
34 be set at fifty percent of the cost of the retirement system.

35 (6) The employee contribution rates for plan 2 under subsections  
36 (3) and (4) of this section shall not include any increase as a result  
37 of any distributions pursuant to RCW 41.31A.020 and 41.31A.030.

1 (7) The required plan 2 and 3 contribution rates for employers  
2 shall be adopted in the manner described in RCW 41.45.060, 41.45.053,  
3 and 41.45.070.

4 (8) The employee contribution rate for members of the public  
5 employees' retirement system plan 2 and school employees' retirement  
6 system plan 2 shall not include any increase as a result of this act.

7 NEW SECTION. Sec. 5. A new section is added to chapter 41.40 RCW  
8 to read as follows:

9 (1) The monthly retirement allowance of a person retiring pursuant  
10 to this act shall be temporarily increased by ten dollars per month per  
11 year of service. This increase shall remain in effect for the first  
12 twenty-four months of the person's retirement.

13 (2) Because of the temporary nature of this section it shall not be  
14 codified.

15 NEW SECTION. Sec. 6. A new section is added to chapter 41.35 RCW  
16 under the subchapter heading "plans 2 and 3" to read as follows:

17 (1) Any member with at least five service credit years who has  
18 attained at least age sixty shall be eligible to retire between  
19 September 1, 2003, and February 29, 2004, and to receive a retirement  
20 allowance computed according to RCW 41.35.400 for plan 2 members or RCW  
21 41.35.620 for plan 3 members, except that a member retiring under this  
22 section shall have his or her retirement allowance reduced by three  
23 percent per year to reflect the difference in the number of years  
24 between age at retirement and the attainment of age sixty-five.

25 (2) The monthly retirement allowance of a member retiring under  
26 this section may be reduced even further as provided in RCW 41.35.220.

27 (3) If a retiree under this section enters employment with an  
28 employer, the retiree's monthly retirement allowance will be reduced by  
29 five and one-half percent for every eight hours worked during that  
30 month up to a maximum reduction of one hundred percent.

31 NEW SECTION. Sec. 7. A new section is added to chapter 41.35 RCW  
32 to read as follows:

33 (1) The monthly retirement allowance of a person retiring pursuant  
34 to this act shall be temporarily increased by ten dollars per month per

1 year of service. This increase shall remain in effect for the first  
2 twenty-four months of the person's retirement.  
3 (2) Because of the temporary nature of this section it shall not be  
4 codified.

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